

**REPORT OF THE AUDIT OF THE
BREATHITT COUNTY
SCHOOL DISTRICT**

**For The Fiscal Year Ended
June 30, 2012**

ROSS & COMPANY, PLLC
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Members of the Board
Breathitt County School District
Jackson, Kentucky

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Breathitt County School District, Jackson, Kentucky, as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirements prescribed by the Kentucky State Committee for School District Audits in Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract - General Audit Requirements, Appendix II to the Independent Auditor's Contract - State Audit Requirements, Appendix III to the Independent Auditor's Contract - Audit Extension Request, and Appendix IV to the Independent Auditor's Contract - Instructions for Submission of the Audit Report. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Breathitt County School District, as of June 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis (unaudited) on pages 3 through 6 and budgetary comparison information on pages 31 through 32 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express

BREATHITT COUNTY SCHOOL DISTRICT
INDEPENDENT AUDITOR'S REPORT
(Continued)

an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Breathitt County School District's financial statements as a whole. The introductory section and combining and individual non-major fund financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. The combining and individual non-major fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements of the Breathitt County School District. The combining and individual non-major fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory section has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Ross and Company", written in dark ink.

Ross and Company, PLLC
November 13, 2012

BREATHITT COUNTY SCHOOL DISTRICT- JACKSON, KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2012

As management of the Breathitt County School District, we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information found within the body of the audit.

FINANCIAL HIGHLIGHTS

- The district gave employees a 1% raise along with step increases.
- The district purchased new hybrid school buses with a grant paying for the hybrid upgrade and the balance financed thru KISTA.
- The General Fund had \$16,924,466 in receipts, which primarily consisted of the state program (SEEK), property, utility taxes, and motor vehicle taxes. This amount also includes on behalf contributions in the amount of \$3,557,526 provided by the state for insurance, KTRS, and vocational school. There was \$17,163,462 in General Fund expenditures including interfund transfers in the amount of \$140,785 to the technology fund and the daycare fund.
- Bonds are issued as the district renovates facilities consistent with a long-range facilities plan that is established with community input and in keeping with Kentucky Department of Education (KDE) stringent compliance regulations.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's financial statements. The District's financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the district is improving or deteriorating.

The statement of activities presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The government-wide financial statements outline functions of the District that are principally supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the District include instruction, support services, operation and maintenance of plant, student transportation and operation of non-instructional services. Fixed assets and related debt is also supported by taxes and intergovernmental revenues.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. This is a state mandated uniform system and chart of accounts for all Kentucky public school districts utilizing the MUNIS administrative

BREATHITT COUNTY SCHOOL DISTRICT- JACKSON, KENTUCKY
MANAGEMENT’S DISCUSSION AND ANALYSIS (MD&A)
JUNE 30, 2012
(Continued)

software. The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into two categories: governmental and proprietary funds. The proprietary funds are made up of the food service and daycare operations. All other activities of the district are included in the governmental funds.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government’s financial position. The districts net assets exceeded the liabilities by \$6,209,888.

The largest portion of the District’s net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, furniture and equipment and construction in progress), less any related debt used to acquire those assets that are still outstanding. The District uses these capital assets to provide services to its students; consequently, these assets are not available for future spending. Although the District’s investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District’s financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

Net Assets for the period ending June 30, 2012

	June 30, 2012	June 30, 2011
Current Assets	\$ 1,830,656	\$ 1,533,073
Noncurrent Assets	15,653,987	16,116,526
Total Assets	17,484,643	17,649,599
Current Liabilities	1,697,345	1,687,689
Noncurrent Liabilities	9,577,410	9,599,347
Total Liabilities	11,274,755	11,287,036
Net Assets		
Invested in capital assets (net of debt)	5,501,142	5,871,980
Restricted	727,428	562,218
Unrestricted	(18,682)	(71,635)
Total Net Assets	\$ 6,209,888	\$ 6,362,563

The following are significant current year transactions that have had an impact on the Statement of Net Assets.

BREATHITT COUNTY SCHOOL DISTRICT- JACKSON, KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
JUNE 30, 2012
(continued)

Comments on Budget Comparisons

- The District's total revenue for the fiscal year ended June 30, 2012 was \$24,995,687, excluding interfund transfers.

The following table presents a summary of revenue and expense for the fiscal year ended June 30, 2012.

Revenue

	Fund 1	Fund 2	Fund 310	Fund 320	Fund 51	Fund 52
Local Revenue Sources	2,534,611	149,871	-	235,555	180,021	52,113
State Revenue Sources	10,699,846	1,595,713	189,419	434,273	15,555	25,073
Federal Revenue Sources	63,367	3,675,951	-	-	1,367,129	-
Interfund Transfers	69,116	37,876	-	-	-	102,909
On Behalf Contributions	3,557,526	-	-	-	183,053	36,611
TOTALS	16,924,466	5,459,411	189,419	669,828	1,745,758	216,706

Expenditures

Amounts include on behalf payments

	Fund 1	Fund 2	Fund 310	Fund 320	Fund 51	Fund 52
Instruction	8,729,241	3,844,857	-	-	-	-
Student Support Services	936,265	29,801	-	-	-	-
Instructional Staff Support Services	634,340	560,770	-	-	-	-
District Admin Support	1,014,537	-	-	-	-	-
School Admin Support	1,025,599	-	-	-	-	-
Business Support Services	323,427	-	-	-	-	-
Plant Operation & Management	2,389,019	103,333	-	-	-	-
Student Transportation	1,822,909	561,899	-	-	-	-
Enterprise Operation	-	-	-	-	-	217,632
Food Service Operations	-	-	-	-	1,774,281	-
Community Services	-	349,966	-	-	-	-
Debt Service	147,340	-	79,758	669,828	-	-
Fund Transfer	140,785	8,785	60,331	-	-	-
TOTALS	17,163,462	5,459,411	140,089	669,828	1,774,281	217,632

General Fund Revenue/Expenditures (Fund 1)

The majority of revenue was derived from State Revenue (84%) with local funding making up 15% of total revenue.

The greatest amount of revenue is spent on instruction expenditures. This makes up 58% of the budget. The instruction function includes the SBDM expenditures for staff and supplies. The student support services make up 5% which includes attendance services, guidance counseling, health services, psychological testing, speech, hearing and vision services. The instructional staff support makes up 3% which includes staff support personnel and librarians. The district administration support makes up 4% which includes workers comp, sick leave pay for retirees, contingency, property insurance, tax collection fees, and superintendent's office expenses. The school administration support makes up 6% which includes principals and secretaries expenses. The business support services makes up 1% which includes the finance office and other central office expenditures. The plant operation and management makes up 12%, student transportation makes up 10% and enterprise/food service operation makes up 1%.

Fund 2 Revenue/Expenditures

The majority of revenue was derived from federal sources (67%) with the state revenue making up 30% and the remaining 3% derived from local sources. The function with the greatest expenditure is instruction being 70%.

Fund 310 and Fund 320 Revenue/Expenditures

Fund 310 is the capital outlay fund and fund 320 is the building fund (FSPK). State funding makes up the Capital Outlay and the building fund is made up of state and local revenue. During the FY12 school year these funds were used to make bond payments on existing debt and to make maintenance repairs.

Fund 360 Revenue/Expenditures

This is the construction fund used for new building or renovations.

Fund 51 Revenue/Expenditures

This is the food service fund. The revenue is received from local, state and federal monies. The largest being federal which makes up 75% of the budget.

Fund 52 Revenue/Expenditures

This is the daycare funds. The revenue is received from parent tuition and state payments.

BUDGETARY IMPLICATIONS

In Kentucky the public school fiscal year is July 1-June 30; other programs, i.e. some federal operate on a different fiscal calendar, but are reflected in the district overall budget. By law the budget must have a minimum 2% contingency. Significant Board action that impacts the finances included a 1% pay raise for all employees.

Questions regarding this report should be directed to the Finance Officer, Darnell McIntosh, at (606) 666-2491 ext 224 or by mail at Breathitt County Board of Education, P.O. Box 750, Jackson, Kentucky 41336.

BREATHITT COUNTY SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS

June 30, 2012

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Breathitt County School District ("District") is the basic level of government, which has financial accountability and control over all activities related to the public school education in Breathitt County School District. The District receives funding from local, state and federal government sources and must comply with the requirements of these funding source entities. Board members are elected by the public and have decision-making authority, the authority to levy taxes the power to designate management, the ability to significantly influence operations and have primary financial accountability for fiscal matters. The District is not included in any other governmental "reporting entity" as defined by GASB pronouncements. In accordance with GASB Standard 14, financial transactions of the following component unit are incorporated in the accompanying financial statements:

Breathitt County Board of Education Finance Corporation – The Breathitt County Board of Education resolved to authorize the establishment of the Breathitt County Board of Education Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Bond Act and KRS 273 and KRS 58.180) as an agency of the Boards for financing the costs of school building facilities. The Board members of the Breathitt County Board of Education also comprise the Corporation's Board of directors.

Basis of Presentation

Government-wide Financial Statements

The statement of net assets and the statement of activities display information about the District as a whole. These statements include the financial activities of the primary government with the exception of fiduciary funds. The statements distinguish between those activities of the District that are governmental and those that are considered business-type activities.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the District and for each function or program of the District's governmental activities. Direct expenses are those that are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular program, grants, and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the District, with specific limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each business segment or governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements

Fund financial statements report detailed information about the District. The focus of governmental and enterprise fund financial statements are on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Non-major funds are aggregated and presented in a single column. Fiduciary funds are reported by fund type.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Accounting

The accounts of the District are organized on the basis of funds or account groups, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, reserves, fund balance, revenues and expenditures or expenses as appropriate. The various funds are summarized by type in the financial statements. The District uses the following funds:

Governmental Fund Types

General Fund - The General Fund is the primary operating fund of the District and accounts for all revenues and expenditures of the District that are not encompassed within other funds. All general tax revenues and other receipts that are not allocated by law or contractual agreements to another fund are accounted for in this fund.

Special Revenue Funds – Special Revenue Funds are used to account for the proceeds of grants from local, state and federal revenue sources that are legally restricted to expenditures for specified purposes. Project accounting is employed to maintain integrity for the various sources of funds. Federally funded grant programs are identified in the Schedule of Expenditures of Federal Awards included in this report.

Construction Fund – The Construction Fund is used to account for all resources including proceeds from bond sales for the authorized acquisition and construction of capital facilities.

Capital Outlay Fund - The Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund receives \$100 per the District's adjusted average daily attendance restricted for use in financing projects as identified in the District's facility plan.

Building Fund - The Facility Support Program of Kentucky Fund (FSPK) accounts for funds generated by the building tax levy required to participate in the School Facilities Construction Commission's construction funding and state matching funds, as applicable. Funds may be used for projects identified in the District's facility plan.

Proprietary Fund Type

The District utilizes the proprietary fund type to account for the major funds that include Food Service and Day Care. The Food Service Fund is used to account for school food service activities, including the National School Lunch Program and the National School Breakfast Program, which are conducted in cooperation with the U.S. Department of Agriculture (USDA). There have not been any amounts that have been recorded for in-kind contribution of USDA commodities on the financial statements, except as required by the Single Audit Act as presented on the Schedule of Expenditures of Federal Awards.

Fiduciary Fund Type

The School Activity Funds are fiduciary funds used to account for student activity organizations in accordance with the Accounting Procedures for Kentucky School Activity Funds. Financial statements of groups and organizations associated with the school system

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fiduciary Fund Type (Continued)

not originated within the District (e.g., Band Boosters, Parent-Teacher Associations, etc.) are not included within school activity funds.

Measurement Focus

The accounting and reporting treatment applied to a fund is determined by its measurement focus. The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of the proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds. All governmental fund types are accounted for using a flow of current financial resources measurement focus. The financial statements for governmental funds are a balance sheet, which generally includes only current assets and current liabilities, and a statement of revenues, expenditures and changes in fund balances, which reports on the changes in net total assets. Proprietary funds and fiduciary funds are reported using the economic resources measurement focus. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary activities.

Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds in the fund financial statements are presented on a modified accrual basis of accounting. Proprietary and fiduciary funds are presented on an accrual basis of accounting.

Exchange and non-exchange transactions – There are two types of transactions: exchange and non-exchange. The method of determining revenue recognition (i.e., accrual v. modified accrual) depends upon the type of exchange as well as source of revenue. Exchange transactions occur when each party receives essentially equal value. Non-exchange transactions occur when one party receives value without directly giving equal value in return.

Modified Accrual - Revenue from non-exchange transactions (e.g., grants, entitlements and donations) must be available to be recognized. These sources of revenue are recognized in the fiscal year in which all eligibility requirements have been satisfied. Under the modified accrual basis of accounting, revenues from exchange transactions are recorded when susceptible to accrual, i.e., both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. For the District, “available” means within sixty days of June 30. Property tax revenue is recognized in the fiscal year for which the taxes are levied. Deferred revenue arises when assets are recognized before a revenue recognition criterion has been satisfied. Grants and entitlements received before eligibility requirements are met are recorded as deferred revenue. Under the modified basis of accounting, expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation, are not recognized in governmental funds.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Accounting (Continued)

Accrual - Under the accrual basis of accounting, revenues are recorded when an exchange takes place. Expenses are recognized at the time they are incurred.

Encumbrance Accounting

Encumbrances for goods or purchased services are documented by purchase orders or contracts. Under Kentucky Law, appropriations lapse at fiscal year end. Encumbrances outstanding at that time are to be either canceled or appropriately provided for in the subsequent year's budget.

Cash and Cash Equivalents

For the purposes of the statement of cash flows, the proprietary fund type considers highly liquid investments with maturity of three months or less when purchased to be cash equivalents.

Inventories

On the government-wide financial statements inventories are stated at cost and are expensed when used.

On fund financial statements inventories are stated at cost. The cost of inventory items is recorded as expenditures in the governmental fund types when purchased.

The food service fund uses the specific identification method and the general fund uses the first-in, first-out method.

Budget

The District is required by state law to adopt a budget annually. The budgetary process accounts for certain transactions on a basis other than generally accepted accounting principles (GAAP). Revenues are recorded when received in cash (budgetary) as opposed to when susceptible to accrual.

(GAAP). Expenditures are recorded when paid in cash (budgetary) as opposed to when susceptible to accrual (GAAP). Once the Board approves the budget, it can be amended. Budget appropriations lapse at year-end.

Fund Balances

The School Board has implemented GASB Statement 54 employing new terminology and classifications for fund balance items.

Non-spendable Fund Balance includes amounts that are (a) not in spendable form, or (b) legally or contractually required to be maintained intact. The "not in spendable form" criterion includes items that are not expected to be converted to cash, for example: inventories, prepaid amounts, and long-term notes receivable. At June 30, 2012, the District had a non-spendable fund balance of \$409,145 for prepaid insurance.

Restricted fund balances arise when constraints placed on the use of resources are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or imposed

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Balances (Continued)

by law through constitutional provisions or enabling legislation. At June 30, 2012, the District had \$136,295 restricted in Capital Outlay Fund.

Committed fund balances are those amounts that can only be used for a specific purpose pursuant to constraints imposed by formal action of the government's highest level of decision-making authority, which, for the District is the Board of Education. The Board of Education must approve by majority vote the establishment (and modification or rescinding) of a fund balance commitment. The District had committed \$181,988 for sick leave in the General Fund June 30, 2012.

Assigned fund balances are those amounts that are constrained by the government's *intent* to be used for specific purposes, but are neither restricted nor committed. The Board of Education allows program supervisors to complete purchase orders which result in the encumbrances of funds. Assigned fund balance also include (a) all remaining amounts (except for negative amount balances) that are reported in governmental funds, other than the general fund, that are not classified as non-spendable and are neither restricted nor committed and (b) amounts in the general fund that are intended to be used for a specific purpose. The district did not have any assigned fund balances.

Unassigned fund balance is the residual classification for the general fund. This classification represents fund balance that has not been assigned to other funds and that has not been restricted, committed, or assigned to specific purposes within the general fund.

The District considers unrestricted amounts to have been spent when an expenditure is incurred for purpose for which both restricted and unrestricted fund balance is available. Also, the District has established the order of assigned, committed, and restricted when an expenditures is incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2. SAFEGUARDING CASH AND CASH EQUIVALENTS

The District's cash and cash equivalents consist of amounts deposited in both interest and non-interest bearing accounts. The depository bank deposits for safekeeping and trust with the District's third party agent approved pledged securities to protect District funds on a day-to-day basis during the period of the contract.

At June 30, 2012, the carrying amount of the District's combined deposits (cash and cash equivalents) including school activity funds was \$1,401,535. Bank balances were deemed excess-collateralization under Kentucky law at the time of the largest combined balance for the year ended June 30, 2012.

The cash deposits held at financial institutions can be categorized according to three levels of risk. These three levels of risk are as follows:

NOTE 2. SAFEGUARDING CASH AND CASH EQUIVALENTS (CONTINUED)

Category 1 Deposits that are insured or collateralized with securities held by the District or by its agent in the District's name.

Category 2 Deposits that are collateralized with securities held by the pledging financial institution's trust department or agent in the District's name.

Category 3 Deposits which are not collateralized or insured.

Based on these three levels of risk, all of the District's cash deposits are classified as Category 2.

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that in the event of a depository institution's failure, the District's deposits may not be returned to it. The District follows the requirement of KRS 41.240(4) and does have a deposit policy for custodial risk. As of June 30, 2012, all deposits were covered by FDIC insurance or a properly executed collateral security agreement.

NOTE 3. PROPERTY TAXES

Revenues and other governmental fund financial resource increments (i.e. bond issue proceeds) are recognized in the accounting period in which they become susceptible to accrual; that is, when they become measurable and available to finance expenditures of the fiscal periods. Property taxes collected are recorded as revenues in the fund for which they were levied. The assessment date of the property taxes is January 1 of each year. The levy is normally set during the September Board meeting. The tax rates are listed as follows: Motor Vehicle \$.492 per \$100, Real Estate \$.406 per \$100 and Tangible \$.406 per \$100. The utility tax rate is 3%. Assuming property tax bills are timely mailed, collection date is the period from October 1 through November 30. Collections from the period October 1 through October 31 receive a two percent discount. The due date is the period from November 1 through November 30 in which no discount is allowed. Property taxes received subsequent to November 30 are considered to be delinquent and subject to a lien filed by the County Attorney.

NOTE 4. RETIREMENT PLANS

Kentucky Teachers' Retirement System

The Kentucky Local School District contributes to the Teachers' Retirement System of Kentucky (KTRS), a cost-sharing, multiple employer defined benefit pension plan. KTRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of employees of the public school systems and other public educational agencies in Kentucky.

KTRS requires that members of KTRS occupy a position requiring either a four (4) year college degree or certification by KY Department of Education (KDE). Job classifications that permit experience to substitute for either of these requirements do not participate in KTRS.

KTRS was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through Chapter 161 Section 990 of the Kentucky Revised Statutes (KRS). KTRS issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report can be obtained by writing to Kentucky Teachers'

NOTE 4. RETIREMENT PLANS (CONTINUED)

Kentucky Teachers' Retirement System (Continued)

Retirement System, 479 Versailles Road, Frankfort, KY 40601 or from the KTRS web site at <http://www.ktrs.ky.gov/>.

Funding policy - Contribution rates are established by KRS. Members who established an account in a state retirement system before July 2008 are required to contribute 10.355% of their salaries to KTRS. Members after July 2008 contribute an additional 0.5%. The Commonwealth of Kentucky is required to contribute 13.105% of salaries for members in a state retirement system before July 1, 2008 and 14.105% of salaries for members who started their account after July 1, 2008. The federal program for any salaries paid by that program pays the matching contributions.

Medical Insurance Plan

Plan description - In addition to the pension benefits described above, Kentucky Revised Statute 161.675 requires KTRS to provide access to post-employment healthcare benefits to eligible members and dependents. The KTRS Medical Insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the medical plan may be made by the KTRS Board of Trustees, the Kentucky Department of Employee Insurance and the General Assembly.

To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS Medical Insurance Fund offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. Once retired members and eligible spouses attain age 65 and are Medicare eligible, coverage is obtained through the KTRS Medicare Eligible Health Plan.

Funding policy - In order to fund the post-employment healthcare benefit, active member contributions are matched by the state at .75% of members' gross salaries. Those who became members before July 1, 2008 contribute 1.25% of salary to the plan. Member contributions are 1.75% of salary for those who became members after July 1, 2008. Also, the premiums collected from retirees as described in the plan description and investment interest help meet the medical expenses of the plan. Additionally, under the Shared Responsibility Plan, the local school district employers pay 0.5% of members' salary for the 2011-2012 fiscal year.

The Breathitt County School District total payroll for the year was \$14,262,082. For the year ended June 30, 2012, the Commonwealth contributed \$1,129,197 to KTRS for the benefit of participating employees. The School districts contributions to KTRS for the year ending June 30, 2012 were \$329,155.

County Employees Retirement System

Plan Description - The County Employees Retirement System (CERS) administered by the Kentucky Retirement System (KRS) is a cost-sharing multiple-employer defined benefit public employee retirement system. The plan provides benefit pension plan coverage for substantially all regular non-certified, full-time employees of each county and Public Schools, and any additional eligible local agencies electing to participate in the System. The participant has a fully vested interest after the completion of sixty months of service, twelve of which are current service. At a minimum, terminated employees are refunded their contributions with credited interest at 3% compounded annually through June 30, 1980, 6% thereafter through June 30, 1986, and 4% thereafter.

NOTE 4. RETIREMENT PLANS (CONTINUED)

County Employees Retirement System (Continued)

CERS through KRS provides for retirement, disability, death, and survivor and health benefits of its members. The KRS annual financial report and other required disclosure information is available by writing the Kentucky Retirement System, 1260 Louisville Road, Frankfort, Kentucky 40601-6124, or by calling (800) 928-4646.

Funding Status and Progress - The Kentucky Retirement System administers CERS based upon employer matching contributions from each county, Public Schools and eligible local agencies electing to participate in the System. The Board of Trustees of Kentucky Retirement Systems determines contribution rates each biennium. The following are CERS non-hazardous contribution rates for the year ended June 30, 2012 member is 5% of their salaries. Participation after September 1, 2008 is at the rate of 6%. The District is required to contribute 18.96 %.

The contribution requirement for CERS for the year ended June 30, 2012, was \$871,898, which consisted of \$684,483 from the District and \$187,415 from employees.

Additional information and historical trend information can be obtained from the Teachers Retirement System of Kentucky and the County Employee Retirement System of Kentucky.

NOTE 5. LIABILITY FOR COMPENSATED ABSENCES

Employees are awarded a maximum of 10 days for 185-day contracts, 11 days for 11-month contracts, and 12 days for 12-month contracts of sick leave annually, based upon employment contract terms and District policy. Sick leave is accrued without limitation. Upon retirement from the school system, a certified and classified employee receives from the District an amount equal to 30% of the value of accumulated sick leave at the current daily rate of pay. At June 30, 2012, the estimate for those employees with 27 or more years of service is \$360,060, in which \$181,988 is short-term and \$178,072 is long term, both recorded on the District-wide financial statements.

NOTE 6. CAPITAL ASSETS

Capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported both in the business-type activities column of the government-wide statement of net assets and in the respective funds.

All capital assets are capitalized at cost or estimated historical cost and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received.

The District maintains a capitalization threshold of \$5,000. The District does not possess any infrastructure.

Improvements are capitalized; the cost of, normal maintenance and repairs that do not add to the value of the asset or materially extend an assets life are not capitalized.

BREATHITT COUNTY PUBLIC SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
June 30, 2012
(Continued)

NOTE 6. CAPITAL ASSETS (CONTINUED)

All reported capital assets are depreciated except land. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives for both general capital assets and proprietary fund assets:

<u>Description</u>	<u>Estimated Life in Years</u>
Buildings and Improvements	40
Land Improvements	20
Technology Equipment	5
Vehicles	5-14
Food Service Equipment	7
Furniture and Fixtures	7
Other	10

	<u>June 30, 2011</u>	<u>Additions</u>	<u>Retirements</u>	<u>June 30, 2012</u>
Governmental Activities:				
Land	\$ 513,837	\$ -	\$ -	\$ 513,837
Land Improvements	1,149,683	-	-	1,149,683
Building & Building Improvement	26,721,690	29,622	-	26,751,312
Technology Equipment	2,322,327	102,883	(37,570)	2,387,640
Vehicles	4,191,943	980,615	-	5,172,558
General Equipment	738,858	25,550	-	764,408
Totals At Historical Cost:	35,638,338	1,138,670	(37,570)	36,739,438
Less Accumulated Depreciation				
Land Improvements	755,760	49,141	-	804,901
Building & Building Improvement	14,129,846	767,206	-	14,897,052
Technology Equipment	1,550,270	356,269	(37,570)	1,868,969
Vehicles	2,789,071	260,365	-	3,049,436
General Equipment	416,475	48,618	-	465,093
Total Accumulated Depreciation:	19,641,422	1,481,599	(37,570)	21,085,451
Governmental Activities Capital Net	\$ 15,996,916	\$ (342,929)	\$ -	\$ 15,653,987
Proprietary Activities:				
Building & Building Improvement	\$ 22,460	\$ -	\$ -	\$ 22,460
Technology Equipment	32,820	-	(1,937)	30,883
General Equipment	383,127	13,510	-	396,637
Totals At Historical Cost:	438,407	13,510	(1,937)	449,980
Less Accumulated Depreciation				
Building & Building Improvement	3,818	898	-	4,716
Technology Equipment	28,747	1,289	(1,937)	28,099
General Equipment	286,230	13,666	-	299,896
Total Accumulated Depreciation:	318,795	15,853	(1,937)	332,711
Proprietary Activities Capital Net	\$ 119,612	\$ (2,343)	\$ -	\$ 117,269

NOTE 7. GENERAL LONG-TERM DEBT AND LEASE OBLIGATIONS

The District is required to make lease payments in amounts sufficient to satisfy debt service requirements on bonds issued by the Breathitt County Public Board of Education Finance Corporation to construct school facilities. Current requirements for principal and interest expenditures are accounted for in the Building Fund in accordance with state law. The District is liable for all issues; however, School Facilities Construction Commission participates by contributing those portions of debt that are appropriated in the State's biennial budget.

Breathitt County School District is contingently liable for the debt listed below under School Facilities Construction Commission (SFCC). The SFCC principal has not been included as bonded indebtedness in the basic financial statements. A Schedule of Total Bonded Debt Maturities follows.

The issue date, original amounts of the issue and interest rates are summarized below:

<u>Bond Issue</u>	<u>Original Amount</u>	<u>Interest Rates</u>	2011			2012	
			<u>Outstanding Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Outstanding Balance</u>	
1998A	2,520,000	4.0-4.25%	\$ 450,000	\$ -	\$ 450,000	\$ -	
2004	1,045,000	1.75-4.5%	795,000	-	730,000	65,000	
2005	710,000	4.0-4.5%	680,000	-	5,000	675,000	
2005R	2,615,000	3.0-3.875%	2,390,000	-	40,000	2,350,000	
2007R	2,690,000	3.5 - 4.3%	2,560,000	-	45,000	2,515,000	
2008	2,850,000	2.9-4.0%	2,675,000	-	60,000	2,615,000	
2012	765,000	1.5-2.375%	-	765,000	-	765,000	
			<u>\$ 9,550,000</u>	<u>\$ 765,000</u>	<u>\$ 1,330,000</u>	<u>\$ 8,985,000</u>	
2003 KISTA	251,554	2.0-3.9%	\$ 46,638	\$ -	\$ 22,857	\$ 23,781	
2004 KISTA	233,696	1.0-3.50%	67,885	-	24,901	42,984	
2005 KISTA	125,649	3.0-3.625%	50,339	-	13,113	37,226	
2009 KISTA			186,024	-	22,019	164,005	
2010A KISTA			143,621	-	17,003	126,618	
2010 KISTA	240,039	2.0-3.90%	240,039	-	25,960	214,079	
2012 KISTA	559,152	2.0-2.625%	-	559,152	-	559,152	
TOTAL			<u>\$ 10,284,546</u>	<u>\$ 1,324,152</u>	<u>\$ 1,455,853</u>	<u>\$ 10,152,845</u>	

Assuming the issues are not called prior to scheduled maturity, the minimum obligations at June 30, 2011 for debt service are as shown in the supplemental Schedule of Total Bonded Debt Maturities, which includes "participation agreements" with the Kentucky School Facilities Construction Commission. The Kentucky General Assembly created the KSFCC for the purpose of assisting local schools in meeting school construction needs. The participation agreement amounts to be assumed by KSFCC are not recorded in the District's basic financial statements.

NOTE 7. GENERAL LONG-TERM DEBT AND LEASE OBLIGATIONS (CONTINUED)

**BREATHITT COUNTY SCHOOL DISTRICT
SCHEDULE OF DEBT PAYMENTS
AS OF JUNE 30, 2012**

YEAR	BREATHITT COUNTY SCHOOL DISTRICT		SCHOOL FACILITIES CONSTRUCTION		TOTAL
	PRINCIPAL	INTEREST	PRINCIPAL	INTEREST	
2013	472,050	271,000	97,950	56,423	897,423
2014	490,891	257,151	99,109	56,029	903,180
2015	512,689	239,459	102,311	52,859	907,318
2016	519,676	220,792	105,324	50,447	896,239
2017	541,573	201,716	108,427	48,082	899,798
2018	558,233	181,602	111,767	45,515	897,117
2019	599,735	150,756	115,265	42,760	908,516
2020	616,011	126,427	118,989	39,817	901,244
2021	642,160	101,325	122,840	36,789	903,114
2022	358,179	88,166	126,821	33,672	606,838
2023	358,905	74,905	131,095	27,979	592,884
2024	374,480	61,600	135,520	22,182	593,782
2025	310,525	47,553	94,475	16,047	468,600
2026	281,746	34,132	98,254	12,268	426,400
2027	282,816	22,862	102,184	8,338	416,200
2028	288,727	11,549	106,273	4,251	410,800
TOTAL	\$ 7,208,396	\$ 2,090,995	\$ 1,776,604	\$ 553,458	\$11,629,453

**BREATHITT COUNTY SCHOOL DISTRICT
SCHEDULE OF KISTA LEASE PAYMENTS
AS OF JUNE 30, 2012**

YEAR	BREATHITT COUNTY SCHOOL DISTRICT		TOTAL
	PRINCIPAL	INTEREST	
2013	183,507	30,558	214,065
2014	157,778	25,505	183,283
2015	127,876	21,727	149,603
2016	117,996	18,687	136,683
2017	121,195	15,826	137,021
2018	119,577	12,723	132,300
2019	120,219	9,520	129,739
2020	95,661	6,142	101,803
2021	72,462	3,501	75,963
2022	51,574	1,354	52,928
TOTAL	\$ 1,167,845	\$ 145,543	\$ 1,313,388

NOTE 8. OPERATING FUND TRANSFERS

The following transfers were made during the year.

Type	From Fund	To Fund	Purpose	Amount
Matching	General	Special Revenue	KETS Offer of Assistance	\$ 37,876
Operating	Special Revenue	General	Indirect Cost	8,785
Operating	Capital Outlay	General	Maintenance Cost	60,331
Operating	General	Child Care	Salary cost	102,909
Total Transfers				<u>\$ 209,901</u>

NOTE 9. RISK MANAGEMENT

Kentucky School Districts Insurance Trust

The District is exposed to various risks related to limited torts; theft of, damage to and destruction of assets; errors and omissions and natural disasters for which the District participates in the Southern States Insurance Fund. The fund is a public entity risk pool, which operates common risk management and insurance programs. Eligible participants include all school Districts and other tax-supported educational agencies of Kentucky who are members of the Kentucky School Districts Association. The District pays an annual premium to each fund for coverage. Dividends may be declared, but are not payable until twenty-four (24) months after the expiration of the self-insurance term. The Liability Insurance Fund pays insurance premiums of participating members established by the insurance carrier. The Trust can terminate coverage by giving ninety days notice. In the event the Trust terminated coverage, any amount remaining in the Fund (after payment of operational and administrative costs and claims for which coverage was provided) would be returned to the member on a pro-rata basis. Except for limitations of coverage for terrorist acts, there have been no significant reductions in coverage from the prior year and settlements have not exceeded coverage in the past three years.

Health Care Coverage

Full-time employees of the District are covered by the State administered medical insurance plan. The State contribution varies depending on the plan, and employees, at their option, authorized payroll withholdings to pay contributions for dependents or increased coverage. Medical and Life insurance coverage paid by the State on behalf of District employees has been recorded as a revenue and expenditure in the General Fund. Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement can put the District at substantial risk.

Worker's Compensation

The District participates in the KSBA. Contributions to the Worker's Compensation Fund are based on premium rates established by such fund in conjunction with the excess insurance carrier, subject to claims experience modifications and a group discount amount.

NOTE 9. RISK MANAGEMENT (CONTINUED)

Unemployment Insurance

The District obtains unemployment insurance coverage through the Kentucky School Districts Insurance Trust Unemployment Compensation Fund; however, the risk has not been transferred to such fund.

NOTE 10. COMMITMENTS AND CONTINGENCIES

Litigation

The Board of Education is the defendant in a number of lawsuits arising principally in the normal course of operations and from alleged illegal acts committed by individual(s) employed by the district and management. The Board is covered by insurance against this type of liability. At this time, the administration is unable to make an evaluation regarding the likelihood of an unfavorable outcome or any possible financial implication to the Board of Education.

Grant Programs

The District participates in numerous state and federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the District has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectability of any related receivable at June 30, 2012 may be impaired. In the opinion of the District, there are no significant contingent liabilities relating to compliance with rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying combined financial statements.

NOTE 11. BUDGETARY DISCLOSURE REQUIREMENTS

Budgetary comparisons for the General Fund and Special Revenue Fund are disclosed as required supplementary information. "On behalf" contributions of \$3,777,190 made by the Commonwealth of Kentucky were recorded in District records as revenues and expenditures. The purpose of the policy change was to conform to requirements of the GASB 34 reporting model. District budget appropriations did not reflect this change in policy. As a result, budget comparisons shown on pages 31 and 32 reflect an excess of both revenues and expenditures over appropriations at the fund level.

NOTE 12. ON-BEHALF PAYMENTS

The District receives on-behalf payments from the State of Kentucky for items including retirement and insurance. The amount received for the fiscal year ended June 30, 2012 was \$3,777,190. These payments were recorded as follows:

General Fund	\$	3,557,526
Food Service		183,053
Day Care		36,611
Total	\$	<u>3,777,190</u>

BREATHITT COUNTY SCHOOL DISTRICT
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2012

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal activity of the Breathitt County School District and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from the amounts presented in, or used in the preparation of, the basic financial statements.

NOTE B – FOOD DISTRIBUTION PROGRAM

Non-monetary assistance is reported in the Schedule at the fair value of the commodities received. Commodities passed through the U.S. Dept. of Agriculture during the year totaled \$77,953 with the USDA providing \$67,953 and \$10,000 received from the U.S. Dept. of Defense.

BREATHITT COUNTY SCHOOL DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year ended June 30, 2012

Section 1. Summary of Auditor's Findings

Financial statements:

Type of auditor's report issued: unqualified

Internal control over financial reporting	Yes	No
• Material weaknesses identified?		X
• Reportable condition(s) identified that are not considered to be material weaknesses?	X	
• Noncompliance material to financial statements noted?		X

Federal Awards:

Internal control over major programs	Yes	No
• Material weakness identified?		X
• Reportable condition(s) identified that are not considered to be material weaknesses?		X None reported

Type of auditor's report issued on compliance for major programs: unqualified

	Yes	No
• Any audit findings disclosed that are required to be reported in accordance with section 510 (a) of Circular A-133?		X

Identification of major programs:

<u>CFDA Numbers</u>	<u>Name of Federal Program or Cluster</u>
10.553, 10.555, 10.559	Child Nutrition Cluster
81.086	Ky Hybrid Electric Bus Program
84.334	GEAR UP

- Dollar threshold used to distinguish between type A and type B programs \$300,000
- Auditee qualified as low-risk auditee? Yes X No

Section 2. Financial Statement Findings

Current Year:

2012-01 Travel Expenses

Statement of Condition: Board paid travel expenses for travel unrelated to Board activities.

Criteria for Condition: Travels expenses must be ordinary, necessary and directly related to school activities.

Cause of the Condition: Tickets to 2012 Boys Sweet 16 basketball tournament along with hotel rooms were purchased with district funds. With Breathitt Co basketball team not participating in the tournament, this activity does not meet the criteria of ordinary, necessary, and/or directly related.

Effect of the Condition: Primarily, a violation of an established Board policy. As a result, district funds were converted to personal use of others.

Recommendation for Correction: The travel policy should be reviewed to ensure awareness of valid travel expenditures.

Management Responses:

The superintendent will not approve travel or any other related expense for any employee to attend Boys Sweet 16 basketball tournament. Travel request will be reviewed to ensure awareness of valid travel expenditures.

2012-02 Construction Projects Lack Required State Approval

Statement of Condition: A required Form BG-1 was not submitted to KDE prior to the construction of the "Batting Cage" at Sebastian Middle School.

Criteria for Condition: Section 162.060 of the Kentucky Constitution relating to school law states, "The chief state school officer shall be furnished a copy of all plans and specifications for new public school buildings." This means all; schools, offices, athletic buildings (including bleacher and stadium seating installation), storage facilities, bus garage or any building being constructed, added onto or renovated regardless of how the work will be funded (including booster projects.) 702 KAR 4:160 establishes the requirements for the capital construction process. All projects are to be initiated with a BG-1 Project Application Form sent to the Kentucky Department of Education, District Facilities Branch for review. Upon review, a determination will be made on how to proceed, but in no case shall work be performed without submission to this office and to the Department of Housing Buildings and Construction.

BREATHITT COUNTY SCHOOL DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
June 30, 2012
(Continued)

Cause of the Condition: Superintendent failed to prepare and submit the required Form BG-1. This is considered to be management's override of controls and accordingly, deemed a reportable significant deficiency in compliance.

Effect of the Condition: Primarily, failure to submit is a statutory violation of Kentucky Administrative Regulations (KAR) and Kentucky Department of Education (KDE) policies. Secondly, failure to submit bypasses an independent, outside review process.

Recommendation for Correction:

The board and all responsible central office personnel should become familiar with the construction approval process and the Form BG-1 requirements. A brief, two page explanation of the BG-1 process has been provided to management. Furthermore, we recommend the acting Facilities Director be named on an official, permanent basis to this position. This position, in addition to its "Physical Plant" and "Security Departments", shall include "Building & Grounds" with the initial and primary responsibility for compliance and supervision for all renovation and new construction projects.

Management Responses:

The board of education has approved an organizational chart with Facilities Director in charge of Building and Grounds which will include completing and submitting BG-1 forms to KDE for all renovations and new construction projects.

Prior Year: No matters were reported

Section 3. Federal Awards Findings and Questionable Costs

Current Year: No matters were reported

Prior Year: No matters were reported

BREATHITT COUNTY SCHOOL DISTRICT
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

Year ended June 30, 2012

Prior Year Findings: None reported

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Members of the Board
Breathitt County School District
Jackson, Kentucky

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

We have audited the basic financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Breathitt County School District, Jackson, Kentucky, as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements and have issued our report thereon dated November 13, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirements prescribed by the Kentucky State Committee for School District Audits in accordance with Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract - General Audit Requirements, Appendix II to the Independent Auditor's Contract - State Audit Requirements, Appendix III to the Independent Auditor's Contract - Audit Extension Request, and Appendix IV to the Independent Auditor's Contract - Instructions for Submission of the Audit Report.

Internal Control over Financial Reporting

Management of Breathitt County School District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Breathitt County School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Breathitt County School District's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned cost that we consider to be

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS
(Continued)

significant deficiencies in internal control over financial reporting, 2012-01 and 2012-02. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

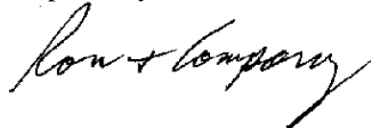
As part of obtaining reasonable assurance about whether the Breathitt County School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards. In addition, the results of our tests disclosed no material instances of noncompliance of specific state statutes or regulation indentified in Appendix II of the Independent Auditor's Contract- State Audit Requirements.

We noted certain other matters that we reported to management of Breathitt County School District in a separate letter dated November 13, 2012.

Breathitt County Public School's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit Breathitt County Public School's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the members of the Breathitt County Board of Education, others within the District, the Kentucky Department of Education, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Ross and Company", written in a cursive style.

Ross and Company, PLLC
November 13, 2012

ROSS & COMPANY, PLLC
Certified Public Accountants
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Members of the Board
Breathitt County School District
Jackson, Kentucky

**INDEPENDENT REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

Compliance

We have audited the compliance of Breathitt County School District with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that could have a direct and material effect on each of Breathitt County School District's major federal programs for the year ended June 30, 2012. Breathitt County School District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Breathitt County School District's management. Our responsibility is to express an opinion on Breathitt County School District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States and Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract - General Audit Requirements, Appendix II to the Independent Auditor's Contract - State Audit Requirements, Appendix III to the Independent Auditor's Contract - Audit Extension Request, and Appendix IV to the Independent Auditor's Contract - Instructions for Submission of the Audit Report. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Breathitt County School District's compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Breathitt County School District's compliance with those requirements.

In our opinion, Breathitt County School District complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

INDEPENDENT REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN
ACCORDANCE WITH OMB CIRCULAR A-133
(Continued)

Internal Control over Compliance

Management of Breathitt County School District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Breathitt County School District's internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Breathitt County School District's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider material weaknesses as defined above.

Breathitt County School District's response to the findings identified in our audit, if any, is described in the accompanying schedule of findings and questioned costs. We did not audit the Breathitt County School District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the audit committee, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Ross & Company", is written over a horizontal line.

Ross & Company, PLLC
November 13, 2012

ROSS & COMPANY, PLLC
Certified Public Accountants
800 Envoy Circle
Louisville, KY 40299-1837
Telephone (502) 499-9088
Facsimile (502) 499-9132

Members of the Board
Breathitt County School District
Jackson, Kentucky

RECOMMENDATION AND COMMENTS TO MANAGEMENT

In planning and performing our audit, we considered Breathitt County School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Breathitt County School District's internal control over financial reporting.

However, during our audit, we became aware of matters that are opportunities for strengthening internal controls and operating efficiency. We previously reported on the District's internal control in our report dated November 13, 2012. This letter does not affect our report dated November 13, 2012, on the financial statements of the Breathitt County School District. The conditions observed are as follows:

Current Year Comments –

2012-01 Travel Expenses

Statement of Condition: Board paid travel expenses for travel unrelated to Board activities.

Criteria for Condition: Travels expenses must be ordinary, necessary and directly related to school activities.

Cause of the Condition: Tickets to 2012 Boys Sweet 16 basketball tournament along with hotel rooms were purchased with district funds. With Breathitt Co basketball team not participating in the tournament, this activity does not meet the criteria of ordinary, necessary, and/or directly related.

Effect of the Condition: Primarily, a violation of an established Board policy. As a result, district funds were converted to personal use of others.

Recommendation for

Correction: The travel policy should be reviewed to ensure awareness of valid travel expenditures.

Management Responses:

The superintendent will not approve travel or any other related expense for any employee to attend Boys Sweet 16 basketball tournament. Travel request will be reviewed to ensure awareness of valid travel expenditures.

BREATHITT COUNTY SCHOOL DISTRICT
RECOMMENDATION AND COMMENTS TO MANAGEMENT
JUNE 30, 2012

2012-02 Construction Projects Lack Required State Approval

Statement of Condition: A required Form BG-1 was not submitted to KDE prior to the construction of the “Batting Cage” at Sebastian Middle School.

Criteria for Condition: Section 162.060 of the Kentucky Constitution relating to school law states, “The chief state school officer shall be furnished a copy of all plans and specifications for new public school buildings.” This means all; schools, offices, athletic buildings (including bleacher and stadium seating installation), storage facilities, bus garage or any building being constructed, added onto or renovated regardless of how the work will be funded (including booster projects.) 702 KAR 4:160 establishes the requirements for the capital construction process. All projects are to be initiated with a BG-1 Project Application Form sent to the Kentucky Department of Education, District Facilities Branch for review. Upon review, a determination will be made on how to proceed, but in no case shall work be performed without submission to this office and to the Department of Housing Buildings and Construction.

Cause of the Condition: Superintendent failed to prepare and submit the required Form BG-1. This is considered to be management’s override of controls and accordingly, deemed a reportable significant deficiency in compliance.

Effect of the Condition: Primarily, failure to submit is a statutory violation of Kentucky Administrative Regulations (KAR) and Kentucky Department of Education (KDE) policies. Secondly, failure to submit bypasses an independent, outside review process.

*Recommendation for
Correction:*

The board and all responsible central office personnel should become familiar with the construction approval process and the Form BG-1 requirements. A brief, two page explanation of the BG-1 process has been provided to management. Furthermore, we recommend the acting Facilities Director be named on an official, permanent basis to this position. This position, in addition to its “Physical Plant” and “Security Departments”, shall include “Building & Grounds” with the initial and primary responsibility for compliance and supervision for all renovation and new construction projects.

Management Responses:

The board of education has approved an organizational chart with Facilities Director in charge of Building and Grounds which will include completing and submitting BG-1 forms to KDE for all renovations and new construction projects.

BREATHITT COUNTY SCHOOL DISTRICT
RECOMMENDATION AND COMMENTS TO MANAGEMENT
JUNE 30, 2012

2012-03 Activity Funds Used For Basic Routine Operations and Maintenance

Statement of Condition: Cleaning supplies should not be purchased with activity fund monies.

Criteria for Condition: School activity funds shall not be used to pay for basic routine operating expenses, renovations or maintenance of school facilities or buildings per Accounting Procedures for Kentucky School Activity Funds, "Redbook."

Cause of the Condition: Purchases were made for cleaning supplies out of general account in the activity funds.

Effect of the Condition: School activity money generated by students may be used to provide student incentives for scholarship, athletics, specialized area performance, school spirit, and similar achievements.

*Recommendation for
Correction:* The board should purchase routine supplies, such as cleaning supplies instead of using individual school activity funds.

Management Responses:

The board of education has approved a budget for schools to purchase cleaning supplies.

2012-04: Handling Cash, (Redbook)

Statement of Condition: All money collected by a teacher/sponsor shall be given to the school treasurer on the day of collection. <WP 55>

Criteria for Condition: All money collected by a teacher/sponsor shall be given to the school treasurer on the day of collection per Accounting Procedures for Kentucky School Activity Funds, "Redbook."

Cause of the Condition: It appears teachers/sponsors held money/checks for a length of time before submitting them to the school treasurer.

Effect of the Condition: Money is not deposited in a timely manner.

*Recommendation for
Correction:* Require teachers/sponsors submit all money collected to school treasurer on date of collection.

Management Responses:

Auditor's recommendation will be followed to ensure funds collected by teachers are submitted to the school treasurer.

BREATHITT COUNTY SCHOOL DISTRICT
RECOMMENDATION AND COMMENTS TO MANAGEMENT
JUNE 30, 2012

2012-05: Individual Accounts in the Activity Funds, (Redbook)

Statement of Condition: Individual accounts should be utilized for activity funds.

Criteria for Condition: The receipts and disbursements of each fund are accounted for separately per Accounting Procedures for Kentucky School Activity Funds, "Redbook"

Cause of the Condition: Activity Funds monies are accounted for in one account, General Fund.

Effect of the Condition: Organizations are not aware of available funds for purchases.

Recommendation for Correction: Each individual organization should have their own account to ensure proper recording of fundraisers and spending.

Management Responses:

Auditor's recommendation will be followed with individual accounts established in the school accounting software.

2012-06: Use of Purchase Orders, (Redbook)

Statement of Condition: Purchase orders were not used for every purchase.

Criteria for Condition: A Purchase Order shall be prepared and approved by the sponsor and principal before the payment is obligated per Accounting Procedures for Kentucky School Activity Funds, "Redbook"

Cause of the Condition: Purchase orders were not utilized for every purchase.

Effect of the Condition: Purchases being made without proper prior approval.

Recommendation for Correction: A purchase order shall be prepared and approved before all purchases.

Management Responses:

Auditor's recommendation will be followed with purchase orders approved for all purchases.

Prior Year Comments

2011-01 Deposits over \$100, (Redbook)

Status: Documents were examined that support timely deposits.

If any action occurs after this exit conference date, which affects the significant or material findings, it is the responsibility of management to provide that information to the auditors.

BREATHITT COUNTY SCHOOL DISTRICT
RECOMMENDATION AND COMMENTS TO MANAGEMENT
JUNE 30, 2012

We sincerely appreciate the courtesy extended to our audit staff again this year. Please feel free to contact us should you have any questions or concerns regarding your audit.

Respectfully Submitted,

A handwritten signature in black ink that reads "Ross and Company". The signature is written in a cursive, flowing style.

Ross and Company, PLLC
November 13, 2012



ADAM H. EDELEN
AUDITOR OF PUBLIC ACCOUNTS

October 10, 2012

Breathitt County Board of Education
P.O. Box 750
Jackson, KY 41339

Members of the Board of Education:

The Auditor of Public Accounts (APA) has completed an examination of the Breathitt County Board of Education (BOE). Our office received concerns related to specific activities and transactions that could indicate possible mismanagement leading to noncompliance with Board policy or state law. This letter summarizes the procedures performed and communicates the results of those procedures.

The APA reviewed certain activities for the period July 1, 2009 through June 30, 2012. The procedures performed include reviewing expenditure transactions, payroll, grant agreements, and general policies and procedures of the BOE. In addition, our review consisted of interviews with various staff and management at the BOE and within the school district.

The purpose of this review was not to provide an opinion on financial statements or activities, but to ensure appropriate processes are in place to provide strong oversight of financial activity and to review specific issues brought to our attention.

Detailed findings and recommendations are attached to this letter to assist all parties involved in improving procedures and internal controls. Overall, these findings indicate the former superintendent exerted a great amount of control without proper oversight of the school board. Due to this level of control beyond the typical authority of a superintendent, BOE and district employees did not have an appropriate outlet for communicating or addressing problems, and were therefore unable to stop or deter poor management practices. In addition to the findings, the BOE's management responses to the findings are included.

If you have any questions, contact me or Libby Carlin, Assistant Auditor of Public Accounts.

Sincerely,

A handwritten signature in black ink, appearing to read "Adam H. Edelen", written over a horizontal line.

Adam H. Edelen

Auditor of Public Accounts

c: Melanie Stevens, Interim Superintendent of Breathitt County Schools

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS**

BREATHITT COUNTY BOARD OF EDUCATION FINDINGS AND RECOMMENDATIONS

2012-01: Employees Were Paid For Extra Days And Wages Without Board Approval

During our examination of the Breathitt County School District's payroll records, we found that employees were paid for more days than authorized by their contract. Extra days paid were approved by the former superintendent, and authorized only at his discretion. We reviewed the minutes of the school board meetings and could not find where the board was informed or approved the extra pay. The Policy and Procedures Manual for the Breathitt County Board of Education says, "Contracts for all certified personnel hired after June 10, 1996 shall not exceed 220 days per fiscal year." The following amounts were paid to employees over their contract terms during the last three years:

- Fiscal year ending June 30, 2010, a total of \$81,814 was paid to 22 employees;
- Fiscal year ending June 30, 2011, a total of \$90,162 was paid to 24 employees; and
- Fiscal year ending June 30, 2012, a total of \$22,951 was paid to 5 employees.

Included in the amounts listed above, the Assistant Superintendent was paid for 20 extra days before his original contract term of 220 days were worked in each of the last three years. The following amounts were paid to the Assistant Superintendent in advance of his working the days, and in excess of his contract terms during the last three years:

- The Assistant Superintendent was paid \$2,985 on November 16, 2009 and \$2,956 on February 15, 2010 for a total of \$5,941 for 20 extra days during fiscal year ending June 30, 2010;
- The Assistant Superintendent was paid \$3,059 on November 15, 2010 and \$3,059 on February 15, 2011 for a total of \$6,118 for 20 extra days during fiscal year ending June 30, 2011; and
- The Assistant Superintendent was paid \$3,090 on October 17, 2011 and \$3,090 on February 15, 2012 for a total of \$6,180 for 20 extra days for fiscal year ending June 30, 2012.

The Buildings and Grounds employee was also paid 20 extra days before his original contract term of 220 days were worked for fiscal years 2009/2010 and 2010/2011. He was paid \$2,985 for 10 extra days each on December 15, 2009 and April 1, 2010, for a total of \$5,970. He was also paid \$3,015 for 10 extra days each on November 1, 2010 and March 1, 2011, for a total of \$6,030. For fiscal year ending June 30, 2012, his contract was changed from a 220 day contract to a 240 day contract by the former superintendent. This resulted in a pay increase of \$6,180.

We also noted the Transportation Director's contract was changed from a 220 day contract to a 240 day contract in January 2010 without the approval of the school board. This resulted in a pay increase of \$4,742.

Also, during fiscal year ending June 30, 2010, seven classified employees were given pay raises by the former superintendent without proper approval by the board. These raises were between \$1 and \$2.12 per hour above the 1% raise given to all classified employees. Subsequently, the former superintendent included these raises in the salary schedule presented to the board two fiscal years later, and therefore the raises were approved by the board on the 2011-12 classified salary schedule. We also found two classified employees were given pay raises of \$1 per hour during the 2011-12 school year that were not approved by the board.

KRS 160.390 requires all personnel actions by the superintendent shall be reported to the board and recorded in the next meeting after the action is taken.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-01: Employees Were Paid For Extra Days And Wages Without Board Approval (Continued)

We recommend:

- All arrangements extending an employee's number of days paid beyond their original contract be authorized by the board prior to the first day the additional work begins.
- Employees not be paid in advance, especially for additional days beyond their contract term before their regular contract days are worked.
- The Superintendent should ensure all personnel actions are reported to the school board as required KRS 160.390.

The school board should research matters reported above, and determine any violations of the board's policies and the most appropriate resolution.

Management's Response and Corrective Action Plan:

This issue has been resolved under the current contract year. All auditors recommendations will be followed. The only certified personnel authorized by the board to work above a 220 day contract are the superintendent, head teachers with the Kentucky Educational Collaborative for State Agency Children (as required and approved in the memorandum of agreement) and the agriculture teacher at Breathitt High School (as required by law). No extension of any number of days will be authorized by the board prior to the first day the additional work begins. Employees were notified by letter that they were not to work days beyond their contract term and that they would not be paid if they did work. Advance pay is not authorized.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-02: Excessive Spending On Boy's Sweet Sixteen Tournament

We reviewed the district's expenditures for the Boy's Sweet Sixteen basketball tournament from July 1, 2009 through June 30, 2012. The amounts spent are excessive and are not a good use of public funds. During this time period, the Breathitt County basketball team did not participate in the tournament. While there were six employees attending training for two days during this period, we found rooms purchased for four or five nights and up to 52 sets of basketball tickets purchased each year, costing the district a net total of \$35,744 during the three year period. Documentation provided shows those attending included the former superintendent, certain members of the school board, other school employees, and members of the general public. We have recapped the spending for each fiscal year as follows:

- For fiscal year ending June 30, 2010, we found that the high school activity fund paid for 36 sets of tickets and the board office paid for 15 sets, totaling \$5,936 for 51 sets of tickets. Also, the board office paid \$18,305 for 16 rooms (eight rooms for four nights and eight rooms for five nights). The total amount spent was \$24,241. We were provided documentation indicating \$7,856 was reimbursed, resulting in a net cost of \$16,385.
- For fiscal year ending June 30, 2011, we found that the high school activity fund paid for 39 sets of tickets and the board office paid for 13 sets, totaling \$6,250 for 52 sets of tickets. Also, the board office paid \$15,422 for rooms. The total amount spent was \$21,672. We were provided documentation indicating \$8,076 was reimbursed, resulting in a net cost of \$13,596.
- For fiscal year ending June 30, 2012, we found that the high school activity fund paid for 20 sets of tickets and the board office paid for 10 sets totaling \$3,610 for 30 sets of tickets. Also, the high school activity fund paid \$4,901 and the board office paid \$2,589 for 10 hotel rooms. The total amount spent was \$11,100. We were provided documentation indicating \$5,337 was reimbursed, resulting in a net cost of \$5,763.

The amounts paid for from the high school activity funds were paid out of the boy's basketball line item. The activity funds should be used for the organization for which they are raised and to benefit the students.

We recommend the Breathitt County Board of Education:

- Review and revise the travel policy to address who may attend the Sweet Sixteen tournament at the district's expense, the specific expenses that may be paid, and the source of funds that will be used to pay the expenses.
- Approve only necessary and reasonable travel expenses.
- Refrain from authorizing expenses for extra tickets for general public and other attendees not required or authorized by the board.

Management's Response and Corrective Action Plan:

Travel policy will be reviewed and revised if necessary to comply with auditors recommendations.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-03: Only Necessary Travel Should Be Paid By The School Board

As discussed in comment 2012-02, the school board paid for hotel rooms and basketball tickets and any reimbursements were received afterwards. Also, we found that the school board paid for the former superintendent and three school board members to attend the national school board association conference in Boston in April 2012. The school board paid for the former superintendent and three school board members' airline tickets and also paid for the airline tickets for each to take a guest with them on the trip. The former superintendent and two of the board members reimbursed the school board for the airline ticket for their guests after the payment was made by the school board. One board member ended up not going on the trip, and therefore the school board was out the unnecessary expense for their guest since this expense has not been reimbursed. Further, we noted the national school board association conference was for three days, but the former superintendent and two school board members were reimbursed meals for 7 days.

The Policy and Procedures Manual for the Breathitt County Board of Education says the school board member shall be reimbursed for actual and necessary expenditures for travel. The school board should not be paying expenditures in advance, then seeking reimbursement for unnecessary expenditures after the fact, such as was the case for guests and basketball tickets. In the future, airline tickets for guests should be paid for by the guests at the time payment is made by the board.

We recommend the school board review the travel policy and stop the practice of paying for unnecessary expenditures up front, then seeking reimbursement afterwards.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-04: State Funding Is Reduced By \$191,000 Due To Instructional Days Not Provided

For the 2011-12 school year, Breathitt County Schools provided 166 instructional days, although the Kentucky Department of Education (KDE) requires a minimum of 177 six-hour instructional days as mandated by the 2012 budget bill. The original calendar submitted for the 2011-12 school year indicated the Breathitt County Board of Education planned to provide 177 regular instructional days. However, the instructional calendar was modified and only 166 instructional days were actually provided. As a result, KDE has indicated it will reduce Breathitt County's SEEK allocation for FY 2013 by approximately \$191,000 for instructional days not provided in FY 2012.

Also, certified teachers in Breathitt County are paid based on a 187 day contract. Teachers worked 166 instructional days plus four professional development days, opening day, closing day, and four paid holidays for a total of 176 total days. Certified teachers were paid the amount as stated on the approved certified salary schedule for 187 days. The amended calendar submitted to KDE from Breathitt County showed 11 equivalent days worked due to the district working 6½ hour days instead of the minimum 6 hour day, however this does not appear to be appropriate method of making up the 11 actual days per KDE guidelines. Therefore, we could not determine that time worked was sufficient to comply with the employees' contracts and the 187 day certified salary schedule approved by the school board. The average teacher's salary for the 2011-12 school year was approximately \$51,474. Teachers were paid for eleven days not actually worked, which result in total wages paid in excess of time worked of approximately \$526,350.

We recommend the Breathitt County Board Of Education ensure that the required instructional days are provided to the students. Also, we recommend the Breathitt County Board of Education determine whether certified employees with 187 day contracts are working the appropriate number of days.

Management's Response and Corrective Action Plan:

The 2012-13 school calendar does contain the appropriate number of days. The 2011-12 school calendar was brought before the board in March and approved to be submitted. We were not aware of the noncompliance until July 18, 2012.

Recommendations of the auditors will be followed.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-05: Breathitt County Board Of Education Meetings Were Not Effective For Proper Oversight

A review of the minutes of the Breathitt County Board of Education meetings indicated the meetings were brief and did not present sufficient information regarding the use of the Breathitt County Board of Education's funds. During the examination, it was reported that the meetings would routinely last around 10 minutes. KRS 160.290(1) states, "Each board of education shall have general control and management of the public schools." We found that most matters of business were included on the consent agenda and approved as a whole and not given individual attention. This increases the risk that non-routine items may be approved by board members without a full understanding of the impact of the transaction or activity. Non-routine items should be separate from the consent agenda.

We also found that the school board was too lenient with oversight over expenditures. Board members were given a claims list for approval without the actual invoices which describe the expenditure. Not having sufficient review and discussion of expenditures has led to excessive and questionable purchases. For example, Sweet Sixteen tickets and other travel related expenditures were paid by credit card and the claims list showed only the name of the credit card company being paid and did not describe the actual charges made.

We recommend the Breathitt County Board of Education:

- Only approve routine items on a consent calendar.
- Discuss and approve non-routine items individually.
- Ensure supporting documentation for expenditures is reviewed in addition to the claims list provided.
- Analyze the APA's 32 Board Recommendations for Public and Nonprofit Boards that were provided by the APA Auditors for those recommendations applicable to the Board, and implement clear policies for those that are appropriate.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

A board member will be assigned to review invoices with the superintendent. The finance officer will supply additional information to the board detailing the nature of the expenditures.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-06: School Based Decision Making Council Should Develop Procedures To Oversee The Activity Fund

As discussed in comment 2012-02, the high school's activity fund purchased tickets and hotel rooms for the Boy's Sweet Sixteen Tournament. We also found that the activity fund at one of the elementary schools was used to pay for sidewalk coating in the amount of \$8,810. In addition, cleaning supplies were purchased out of the activity funds at all schools. The *Accounting Procedures for Kentucky School Activity Funds* (Redbook) says the School Based Decision Making Council (SBDM) should participate in the formulation of policies and procedures concerning activity funds. Also, the SBMD should approve the activity fund budget. The SBMD at each school should determine if the school activity fund policy is consistent with board policy. The activity funds should be used for the organization for which they are raised. The monies generated from bookstore sales, snack and beverage sales, and other office activity funds not raised by a school organization for a specific purpose should be used for the benefit of the students. The tickets and hotel rooms purchased for the Boy's Sweet Sixteen Tournament was paid from the boy's basketball line item of the high school activity fund. This line item should be used to support the boy's basketball team.

We recommend the SBDM develop policies and procedures to oversee the activity fund of each school to ensure that expenditures are used for the benefit of the students and consistent with board policy.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

2012-07: Booster Organizations Should Submit Budget Worksheets And Annual Financial Reports

The booster organizations for Breathitt County Schools did not submit budget worksheets to the principal and only two submitted annual financial reports for the year ending June 30, 2012. The *Accounting Procedures for Kentucky School Activity Funds* (Redbook) requires all booster organizations to submit budget worksheets to the principal within the first thirty days of the school year or within thirty days of the first transaction of the group. Also, booster organizations are required to submit annual financial reports to the principal by July 25 for the year ending June 30. The annual financial report should contain receipts from admissions, fundraisers, dues, concession sales, and other categories; expenditures by payee; and beginning and ending balances. The principal or other designated person should review the budget worksheets and annual financial statements to determine if they are reasonable and report any suspicious activity to the superintendent. We recommend the all booster organizations be informed of the requirements of the Redbook and the school board should ensure those requirements are being met.

Management's Response and Corrective Action Plan:

We will ensure that all booster organizations are informed of the Redbook and school board requirements.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-08: The Former Superintendent Did Not Have A Written Contract For Three Years

The former superintendent was hired on July 1, 2005, for a period of four years. On September 23, 2008, the Breathitt County School Board approved to “extend the superintendent’s contract for four years when the current contract expired with \$10,000 per year raise and ratification in July 2009.” On April 28, 2009, the Breathitt County School Board approved the superintendent’s new four year contract to begin on July, 1, 2009; however, no contract was attached or contract terms disclosed in the board minutes. A written contract was not executed and signed by the former superintendent until May 10, 2012. The former superintendent resigned on May 10, 2012. There was no written contract signed by the superintendent from July 1, 2009 through May 9, 2012. During this time period, he received a salary increase of \$10,000 each year as well as the same percentage increase provided to all other certified personnel. Also, the school board paid for his portion of the Kentucky Teacher’s Retirement contribution. The approval in the minutes of the school board did not specify whether the former superintendent was to receive the same percentage increase provided to all other certified personnel as well as his portion of the retirement contribution. The retirement contribution was paid directly to the teachers’ retirement system and was not considered a taxable fringe benefit on the former superintendent’s W-2.

We recommend the Breathitt County Board of Education:

- Ensure all employment contracts are written and signed prior to the period of the contract.
- Include the executed contract or terms of the contract in the minutes of the board meetings.
- Consult with the IRS to determine whether the retirement contribution paid on behalf of the former superintendent should be a taxable fringe benefit.

Management’s Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

Finance Officer has contacted IRS to determine if the retirement contribution is a taxable fringe benefit.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-09: Years Of Experience For New Employees Could Not Be Substantiated

During our examination of the Breathitt County School District's personnel records, we found that the years of experience for eight new classified employees hired between July 1, 2009 and June 30, 2012 could not be substantiated. Each year the school board approves a salary schedule for classified positions based on years of experience. The personnel files for two employees did not have adequate documentation of the years worked. For the six employees that did have documentation of prior work experience, the experience was not with a school district, was not related to the position hired, or the employee was given more years of experience than the file documented.

In one instance, an employee was given 25 years of experience as a cook/baker even though documentation showed she had worked 14 years in auto parts sales, delivery, and billing. Another instance had an employee receiving 25 years of experience as a custodian; however, records showed that he had only 10 years experience as a security guard. This resulted in the pay rate for these positions to be between \$1.21 and \$3.77 per hour greater than the same position with zero to three years experience. The years of experience were only approved by the former superintendent.

We recommend the school board implement a clear policy on hiring new employees with years of experience, and detailing the types of work that may be considered, and permitting no more than a year-for-year service credit. Also, we recommend that the personnel files adequately document the years worked and justification for the service credit awarded.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

2012-10: Adjustments Made To The Extra Co-Curricular Salary Schedule Should Be Approved By The School Board

The school board approves an extra co-curricular salary schedule each year that includes amounts paid to each individual coach and assistance coach. We found that the amounts paid to the assistant coaches did not agree to the salary schedule approved by the school board. After approval by the school board, the Athletic Director would reapportion the amount paid to each assistant coach. While the total amount approved for assistant coaches was not exceeded, the amounts paid to the individual coaches did not agree to the approved schedule.

We recommend that assistant coaches be paid in accordance with the approved schedule and any adjustments should be presented to the school board for approval.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

**BREATHITT COUNTY BOARD OF EDUCATION
FINDINGS AND RECOMMENDATIONS
(Continued)**

2012-11: Coal Severance Expenditures Should Be Properly Documented

The Breathitt County School Board received a Local Government Economic Development Fund/Single County Coal Severance Grant in the amount of \$200,000. These funds were to be used to purchase tile and equipment to fill in the riverbed adjacent to the Breathitt County High School to expand and improve the campus area. The school had originally sent a quote for drainage tile in the amount of \$200,000 to the Department for Local Government and the funds were sent to the school board. However, the tile was never purchased and the project was put on hold. The grant was then amended to include district wide HVAC improvements, blacktopping improvements, playground equipment, fuel tank and land surveys. As of August 21, 2012, the school has only submitted documentation for \$165,691 of expenditures for this grant after the modifications. The grant agreement requires the school board to submit documentation for expenditures of the project and a project completion report. If a project completion report and documentation for the remaining \$34,309 is not sent to the Department for Local Government, the school board may have to pay this amount back.

We recommend the school board ensure the requirements of the grant are being met and submit a project completion report and documentation for the remaining \$34,309 to the Department for Local Government.

Management's Response and Corrective Action Plan:

Recommendations of the auditors will be followed.

The Department for Local Government has been contacted regarding this issue. Proper documentation and reports will be submitted.